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SENSITIVE
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COMMERCE FOR 4331/MAC/WH/MCAMERON
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ENERGY FOR GWARD, SBROWNE AND RDAVIS
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SUBJECT: PERU ENERGY BRIEFS - MAY 2008

SENSITIVE BUT UNCLASSIFIED, HANDLE ACCORDINGLY

SUMMARY

1. (U) This is an update on the following energy sector news from Peru:
-- New Environment Minister sets conditions for sustainable biofuels development;
-- Brazil and Peru sign 10 agreements on margins of EU-LAC Summit, including biofuels;
-- Brazilian firms to build \$2 billion hydroelectric plant in Peru to export power to Brazil;
-- State-owned Brazilian and Peruvian companies explore petrochemical project;
-- Another U.S. company submits proposal to build a natural gas pipeline to southern Peru; and,
-- GOP ends subsidies to 95- and 97-octane gasolines.
End Summary.

SUSTAINABLE BIOFUELS ONLY

2. (U) The head of Peru's newly created Ministry of the Environment, Minister Antonio Brack, wasted no time after being sworn in on May 16 in beginning to set guidelines for the future work of his agency. To prevent biofuels production from creating a food production and price crisis, Brack set three conditions for their development:
-- trees can not be felled in primary forests to make room for biofuel crops;
-- no biofuel crops can be grown on lands currently producing food crops, and,
-- biofuel crops cannot be watered by flooding -- as is usual in Peru's coastal and highland farmlands -- and must instead use efficient irrigation techniques (drip, pressure, etc.).

BRAZIL AND PERU AGREEMENTS

3. (U Presidents Garcia and "Lula" da Silva (Brazil) signed ten cooperation agreements after the Peru-hosted European Union - Latin

American and Caribbean summit ended on May 17. One of these, the Energy Integration Agreement, provides for the development of hydroelectric projects in Peru for the export of power to Brazil. The other complementary agreements include one to promote alternative biofuels crops and one on the sustainable management of Amazon forests.

BRAZILIAN FIRMS PLAN A \$2 BILLION HYDROELECTRIC PLANT

¶4. (U) Brazilian firms Furnas Centrais Eletricas and Construtora OAS Ltd. have filed an application with Peru's Energy and Mines Ministry (MEM) for a temporary concession to build a \$2 billion hydroelectric plant at Inambari, in the Madre de Dios department bordering with Brazil. The companies plan to carry out a feasibility study so as to eventually obtain a definitive concession. Brazil's Mines and Energy minister Edson Lobao said the plant's capacity would be 3,400 megawatts/hour. Construction of the plant would begin in 2009, and operations would start up in 2012, with all of the power produced bound for export to Brazil.

BRAZIL-PERU PETROCHEMICAL PROJECT

¶5. (U) Presidents Garcia and Lula also witnessed the signing of a Memorandum of Understanding between Petroperu (Peru's state-owned petroleum company) and the Brazilian companies Petrobras and Braskem, whereby the companies will evaluate the economic and technical feasibility to implement in Peru an integrated petrochemical project to produce ethylene and polyethylene.

¶6. (SBU) Project sponsors hope the gas will come from the Camisea

project, but this is far from certain. It is unclear what the contribution of Petroperu will be as the company is relatively small and lacks in-house technical manpower and the financial capability required to undertake major projects. Petroperu already has agreements with Petrobras for the development of a fertilizer petrochemical plant (2007) and for the "technical evaluation" of six blocks in the Marañon basin (2006). (Note: Technical evaluation agreements often lead to entering into regular exploration and production contracts with the licensing agency Perupetro. End note.)

THREE COMPANIES VIE FOR SOUTHERN GAS PIPELINE

¶7. (U) A third company, Texas-based Energy Transfer Inc., has joined two other companies that want to build a natural gas pipeline linking Camisea with the southern port of Ilo, close to the Chilean border. Associated with Panda Energy (U.S.), Energy Transfer is proposing to build the pipeline along the same route earlier proposed by Conduit Capital Partners' Kuntur Transportadora de Gas, i.e. through the highlands passing through Cuzco, Puno and Arequipa to end at the port of Ilo. This route is strongly supported by the presidents of the local regions the pipeline would cross and serve. France's Suez Energie filed an application with the Ministry of Energy and Mines for a temporary concession (while it conducts a feasibility study) for a \$800 million pipeline from Humay (Ica, close to Pisco) along the coast to Ilo, but the company has recently also offered to build the pipeline along a route that passes through the highlands.

SUBSIDIES TO HIGH-OCTANE GASOLINE TO END

¶8. (U) The MEM published a resolution May 20 ending the subsidies to 95- and 97-octane motor gasolines. The GOP will maintain the subsidies to all other fuels. Subsidies were given through the "Price Stabilization Fund for Petroleum Products Fuels." The GOP established the fund in 2004 to prevent the full effect of world crude oil prices being passed on to consumers when prices increased, with GOP funds to be recovered when prices decreased. The 95- and 97-octane gasolines are used by a small number of quality automobiles, such as luxury sedans and recent SUV and minivan models, mostly located in Lima.

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